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IN THE

Supreme Court of the United States

OCTOBER TERM, 1962

No. 62

NORTHERN NATURAL GAS COMPANY, A Corporation,
Appellant,

v.

STATE CORPORATION COMMISSION OF THE STATE OF KANSAS, *Appellee*.

On Appeal from the Supreme Court of Kansas

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE OF THE MID-CONTINENT OIL & GAS ASSOCIATION IN SUPPORT OF APPELLEE, AND BRIEF AMICUS CURIAE BY THE MID-CONTINENT OIL & GAS ASSOCIATION

R. J. STANTON
W. W. HEARD
1107 Pan American Building
511 South Boston Avenue
Tulsa, Oklahoma
Attorneys for Mid-Continent Oil & Gas Association

November 12, 1962

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE OF THE MID-CONTINENT OIL & GAS ASSOCIATION IN SUPPORT OF APPELLEE

Movant, Mid-Continent Oil & Gas Association, pursuant to the provisions of Rule 42 (3) of this Honorable Court, respectfully moves that it be granted leave to file the accompanying brief amicus curiae in this case. The consent of the appellee has been obtained. The consent of appellant was requested but refused.

The Mid-Continent Oil & Gas Association has approximately 8,500 members, with its principal office in Tulsa, Oklahoma. The members of this Association are actively engaged in one or more phases of the oil and gas industry. The Association is principally concerned with matters relating to the production phase of the industry, and consequently the Association has been and is now particularly concerned with the ef-

fective administration of the conservation laws of the various oil and gas producing states.

The Association is vitally concerned with the outcome of this case because if this Court now determines that the states may not regulate the production of gas in order to protect the correlative rights of the owners thereof if such regulation incidentally affects sales of gas in interstate commerce, then the anarchy that existed in the production of oil and gas prior to the adoption of conservation laws by the producing states may again, ultimately, prevail.

It is not the purpose of the accompanying brief to argue in detail the specific issues of this case; that has been ably and correctly done by appellee. It is the purpose of the brief to point out to the Court that a decision in favor of the appellee is required if the oil and gas producing states are to be able, in the future, to administer, effectively, the oil and gas conservation policies with which they have been entrusted.

Wherefore, Movant prays that this Court grant this motion and permit the filing herein of the attached brief in support of appellee.

Respectfully submitted,

MID-CONTINENT OIL & GAS ASSOCIATION

By R. J. STANTON

W. W. HEARD
1107 Pan American Building
511 South Boston Avenue
Tulsa, Oklahoma
Attorneys for Mid-Continent Oil & Gas Association

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BRIEF AMICUS CURIAE BY THE MID-CONTINENT OIL & GAS ASSOCIATION

INTEREST OF AMICUS CURIAE

The interest of the Amicus in this case is set forth in the motion to which this brief is attached.

QUESTION PRESENTED

The broad question inherent in this case is whether the Natural Gas Act preempts the authority of the states to regulate the production of gas within their boundaries for the purpose of preventing waste and protecting the correlative rights of the owners thereof.

STATEMENT

On October 7, 1959, and on February 3, 1960, the State Corporation Commission of Kansas, after due notice and public hearing, issued the Orders and Rule involved in this case. The Rule provides for the ratable production of gas from each common source of supply under proration by the Commission by requiring each purchaser to take gas in proportion to the allowables from all the wells to which it is connected. In promulgating such Rule the Commission found that the Rule met the *mandate* of G. S. 1949, 55-703, as amended, which directs the Commission to "so regulate the taking of natural gas from any and all such common sources of supply within this state as to prevent the inequitable or unfair taking from such common source of supply by any person, firm or corporation and to prevent unreasonable discrimination in favor of any one common source of supply as against another and in favor of or against any producer in any such common source of supply." This statute is the Kansas Gas Conservation Act, and the purpose of the portion thereof quoted above is to implement the conservation laws of the state by protecting the correlative rights of the owners of gas in a common source of supply. 1 Summers, Oil and Gas (perm. ed.), Sec. 63, pp. 180-181.

The term "correlative rights of the owners of gas in a common source of supply" connotes property rights. The term merely means that each owner in a common source of supply is entitled to the opportunity to produce, as a property right and in an amount determined by the state, his just and equitable share of gas from the common source of supply; and that no owner has the right to take an undue proportion of such common source of supply.

As early as 1900 this Court in the landmark case of *Ohio Oil Co.* v. *Indiana*, 177 U.S. 190, recognized that the correlative rights of the owners of oil and gas in a common source of supply are property rights upon which the legislative power of the states may be "manifested for the purpose of protecting all the collective owners, by securing a just distribution, to arise from the enjoyment, by them, of their privilege to reduce to possession, and to reach the like end by preventing waste."

There is no longer any serious question that the states have the power, consistent with the commerce clause and the due process clause of the Fourteenth Amendment, to protect the correlative rights of the owners of oil and gas in a common source of supply by requiring the ratable taking thereof. This power of the states has been consistently upheld as a proper exercise of authority to implement the public interest of the states in the conservation of oil and gas. *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U. S. 179 (1950); *Bandini Petroleum Co.* v. *Superior Court*, 284 U. S. 8 (1931); *Champlin Refining Co.* v. *Corporation Commission*, 286 U. S. 210 (1932).

Thus, for many years, the legislatures of the oil and gas producing states have manifested their powers to protect the correlative rights of the owners of oil and gas in a common source of supply. This power has been exercised by these legislatures in various forms; sometimes by declaring all purchasers in a common source of supply to be common purchasers, *e.g.*, 52 *Oklahoma Statutes Annotated*, Section 240, and sometimes by delegating to a state regulatory agency authority to protect correlative rights by appropriate rules and regulations such as Kansas has done here. Whatever

may be the means selected by these legislatures to protect correlative rights, all are legitimate exercises of state legislative power, and it is submitted that the Kansas Orders and Rule in question are no exception.

It is clearly evident from the record in this case that the Commission issued the ratable take Orders and Rule in order to prevent drainage as among Kansas owners while still allowing them to produce their fair share of the total gas in the reservoir. As the Kansas Supreme Court noted at 362 P. 2d 601:

> "We do not read the record to show that there is any contention but that drainage was occurring, and that the under-produced wells were losing the right to produce gas from the common source of supply to the great damage of the owners of the wells in the loss of their correlative rights."

A ratable take order requires each purchaser to take gas from all wells to which it is connected in proportion to the allowables of the wells. Such an order does not require the purchaser to take any particular volume of gas but only that its taking of gas must be apportioned among the various wells to which it is connected. In other words, ratable take orders are designed to prevent discrimination by purchasers against the owners and producers from which they are taking gas from a common source.

Although appellant maintains that the Orders and Rule herein are invalid since they attempt to regulate the sale of gas in interstate commerce simply because they are directed toward purchasers, the facts are that the Orders and Rule do not attempt to regulate any of the aspects of a sale by a producer to a pipeline purchaser. These Orders and the Rule *do not* direct a purchaser to take *any volume* of gas, *at any time* or *at any*

price. All that these Orders and Rule do is to direct purchasers to take proportionately from all wells to which they are connected in order that each owner will be able to produce and enjoy his fair share of the common source of supply. That the Orders and Rule are directed toward purchasers does not change this fact. Ratable take orders must necessarily be directed toward purchasers if the correlative rights of owners of gas are to be protected. The Kansas Supreme Court correctly noted this fact at 362 P. 2d 603 when it stated that:

> "We believe Northern is mistaken in arguing that the above statute and the rules made thereunder do not apply to a purchaser of natural gas. We are only more convinced that the legislature had this in mind, by the fact that natural gas cannot be produced unless someone is ready to buy it, it cannot be stored in a tank on the lease. Therefore, as Professor Summers says, the object of the quoted provisions of section 55-703, cannot be accomplished unless the taker or purchaser can be controlled. We believe the statute is sufficient to reach Northern."

Undoubtedly, the Orders and Rule in question are a valid exercise of the power of the State of Kansas to protect the correlative rights of the owners of gas in a common source of supply located within its boundaries, unless this power was taken from the states by Congress when it enacted the Natural Gas Act, 15 U.S.C.A. 717 et seq.

It is submitted as beyond question that the Natural Gas Act does not preempt the field of regulation to the *complete* exclusion of otherwise valid state action relating to conservation of oil and gas. The Natural Gas Act does not completely preempt the field of regulation by the states.

Section 1 (b) of the Natural Gas Act, 52 Stat. 821 (1938), 15 U.S.C. 717 (b), provides as follows:

> "The provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation or sale, but *shall not apply* to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution *or to the production or gathering of natural gas.*" (Emphasis supplied)

This Court has held, in interpreting this section of the Act, in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U. S. 672 (1954), that, "There can be no dispute that the overriding Congressional purpose was to plug the 'gap' in regulation of natural gas companies resulting from judicial decisions prohibiting, on federal constitutional grounds, state regulation of many of the interstate aspects of the natural gas business." In other words, the purpose of the Act is to provide a regulatory scheme in the areas where the states are not constitutionally competent to act. It is equally clear that it was not the purpose of Congress to preempt the authority of the states in areas where they are constitutionally competent to act, and thus this Court has held that the purpose of the production and gathering exemption of Section 1 (b) of the Act is to preserve in the states powers of regulation in areas in which the states are constitutionally competent to act. *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 498 (1949); *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U.S. 581 (1945);

Interstate Natural Gas Co. v. Federal Power Commission, 331 U.S. 682 (1947); *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944).[1] It has been shown above that the power of the states to protect the correlative rights of the owners of oil and gas in a common source of supply is within an area in which the states are constitutionally competent to act. It should, therefore, be equally clear that the power to implement the conservation of oil and gas by the protection of correlative rights has been preserved to the states and withheld from the jurisdiction of the Federal Power Commission by Section 1 (b) of the Act.

The Federal Power Commission itself, contrary to its Memorandum in response to this Court's order of

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[1] In *Hope*, 320 U.S. 612-613, the Court stated:

> ". . . the Act does not intrude on the domain traditionally reserved for control by state commissions; and the Federal Power Commission was given no authority over 'the production or gathering of natural gas.' § 1(b). In addition, Congress recognized the legitimate interests of the States in the conservation of natural gas. By § 11 Congress instructed the Commission to make reports on compacts between two or more States dealing with the conservation, production and transportation of natural gas. The Commission was also directed to recommend further legislation appropriate or necessary to carry out any proposed compact and 'to aid in the conservation of natural-gas resources within the United States and in the orderly, equitable, and economic production, transportation, and distribution of natural gas.' § 11(a). Thus Congress was quite aware of the interests of the producing states in their natural gas supplies."

Interstate, *Colorado Interstate*, *Panhandle* and *Phillips* reaffirm that the Act does not intrude on the domain traditionally reserved for control by state commissions, and thus "accordingly, Congress in § 1 (b) of the Act not only prescribed the intended reach of the Commission's power, *but also specified the areas into which this power was not to extend.*" *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 503. (Emphasis supplied)

March 19, 1962 (369 U.S. 814), has recognized that it has no jurisdiction over matters relating to the ratable production of natural gas, the correlative rights of producers and proration of production among producers producing natural gas from common reservoirs. See Appendix A, *Order Denying Petition for Leave to Intervene* issued October 17, 1962, *Lone Star Gas Gathering Company*, Docket No. CP62-179. As stated by the Commission in this Order:

> "We have carefully considered the allegations of Petitioner and the answer thereto filed by Lone Star. The matters upon which Petitioner desires to be heard in this proceeding relate to the ratable production of natural gas, the correlative rights of producers and proration of production among producers producing natural gas from common reservoirs. *We are of the opinion that these are matters which lie within the sphere of state control and cannot constitute a basis for intervention in the proceedings before this Commission.*" (Emphasis supplied)

We submit that the Federal Power Commission is eminently correct that matters *relating* to the *ratable* production of natural gas, which necessarily includes the taking thereof, are matters which are within the sphere of state control *and not within the sphere of federal control.* If this is so and this Court holds, as appellant would have it do, that the Orders and Rule here in question are invalid because being directed toward purchasers they affect sales of gas in interstate commerce, then a "gap" will be created in the comprehensive scheme of regulation intended by Congress when it passed the Natural Gas Act for the reason that, then, neither the states nor the Federal Power Commission could thereafter *act* over matters relating

to the ratable production of natural gas, the correlative rights of producers and proration of production.

The Kansas Orders and Rule in question in this case lie within the sphere of state control even though the Orders and Rule are directed to purchasers of natural gas from each common source of supply. The gist of appellant's argument is that because the Orders and Rules are directed toward purchasers they constitute an attempt by Kansas to regulate the sale of gas in interstate commerce. Nothing could be further from the truth.

State orders requiring ratable purchase or takes are designed to protect the correlative rights of producers in a common source of supply. This fact has been recognized by an eminent authority in the field of oil and gas law:

> "Statutes making pipe line companies common purchasers of oil and gas are, in purpose and effect, conservation measures, and so operate, whether the production of oil or gas from a common source of supply is or is not restricted and prorated among the wells therein for the prevention of waste. Courts in most of the oil and gas producing states have held that a state may validly legislate for the prevention of waste of oil and gas and for the protection of the correlative rights of owners and lessees, in a common source of supply. Legislative enactments and judicial opinions have repeatedly stated that conservation measures and the orders and regulations of conservation agencies should be such as to afford the owner of each tract of land in a common source of supply of oil or gas the opportunity to produce his just and equitable share of the oil or gas therein and to use therefor his just and equitable share of the reservoir energy. Unless all the producers in a common source of supply

> have equal opportunity to sell or to transport oil and gas from their wells, they are not afforded the opportunity to produce their just and equitable share of the oil or gas or to utilize their just and equitable share of the reservoir energy." (4 Summers, *Oil and Gas*, Perm. Ed., Sec. 754, p. 182)

Although the Kansas statute is not a "common purchaser" statute in that it does not expressly state that purchasers of gas in a common source of supply may be required to take ratably from all wells to which they are connected, the Kansas Court in this case correctly noted that unless the Commission has such authority it cannot prevent inequitable and unfair taking and *prevent discrimination in favor of or against any producer* in the common source of supply.

Whether the oil and gas producing states endeavor to protect correlative rights by enacting common purchaser statutes or by general statutes such as the Kansas statute, is immaterial. The point is that the power preserved to the states under the Natural Gas Act to protect the property interests of all the owners of a common source of supply can be effectuated *only* by requiring the purchasers receiving gas from such common source of supply to take proportionately from all of the wells to which each may be connected.[2] This is

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[2] Appellant, at page 19, footnote 1 of its Brief, states that a state may restrict the production from developed leases for the purposes of conservation *and protection of correlative rights.* (Emphasis supplied) It would therefore appear that appellant concedes that the power to protect correlative rights has been preserved to the states. This concession, as stated by appellant, is, however, illusionary. Orders of a state establishing allowable production from the wells in a field in no way assure an owner of such production that his interest will be produced and taken. Appellant, therefore, concedes the power of the states to protect correlative rights but would deny to the states the means of implementing that power.

all that the Orders and Rule complained of are designed to do.

The Federal Power Commission recognizes that the property interests of the owners of gas in a common source of supply can be protected by the state only by requiring pipeline purchasers to take proportionately from all wells to which each may be connected and that therefore state ratable take orders *relate to production*. Such recognition by the Federal Power Commission is indicated by its Memorandum, at page 25, where it is stated:

> "The natural gas industry differs from other industries in that *the production* of the commodity (i.e., the withdrawal of gas from the well) and its movement into interstate channels constitute one and the same physical operation. Thus, a regulation limiting the volume a pipeline may purchase from a given well would be tantamount in effect to a limitation upon the production of that well."

And, obviously, this statement is consistent with the view of that Commission that these matters (*i.e.*, ratable, production of natural gas and protection of correlative rights) are within the sphere of state control; that is, these matters fall within the "production and gathering" exemption of Section 1 (b) of the Act.

It thus appears to be undisputed that (1) the states have the constitutional power to require purchasers to take gas ratably from all wells to which they may be connected in a common source of supply in order to protect the correlative rights of the owners thereof; (2) this power of the states was not preempted by Congress when it passed the Natural Gas Act; and (3) *in general*, orders and regulations of a state, imple-

menting that power, fall within the "production and gathering" exemption of Section 1 (b) of the Act.

The Federal Power Commission, however, goes further and argues that the *particular* Kansas Orders and Rule in question do not fall within the "production and gathering" exemption of Section 1 (b) of the Act. The Commission argues that Northern cannot comply with the Orders and Rule in question without incurring, under take or pay for provisions of its contracts, additional costs which "would ultimately fall upon the consumers" (Federal Power Commission Memo., pp. 25-28). It therefore concludes that these Orders and Rules "measured by their practical consequences (still assuming that they provide no relief from contract obligations) are plainly a regulation of sales for resale in interstate commerce."

However, the "impact" on Northern, upon which the Federal Power Commission bases its position, would appear to be not the result of the Kansas ratable take orders, but rather the result of Northern's own contractual arrangements, which were presumably entered into with knowledge that mineral owners possess correlative rights in common sources of supply and that the states have authority to protect those rights. The ultimate consumer will not necessarily bear the impact of any increased costs which may result from Northern's contractual arrangements if such arrangements are deemed improvident by the Federal Power Commission. See *Federal Power Commission* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *Mississippi River Fuel Corp.* v. *Federal Power Commission*, 252 F. 2d 619 (D.C. Cir. 1957), *cert. den.*, 355 U.S. 904 (1957). Further, there is nothing in the record to show that Northern will not be able in the future to comply with

both the ratable take order and the take requirements of its contracts. As a matter of fact, the record is also barren of any evidence that Northern will not be able to take without further cost all gas previously paid for, but not taken.[3]

In effect, what the Federal Power Commission simply says, as did appellant in the Kansas Court, is that the *valid* orders of a state requiring ratable takes of gas from a common source of supply *are unenforceable* against interstate pipeline companies if such orders are incompatible with the contractual obligations of the pipeline with its producer supplier. In other words, as stated by the Kansas Court below, 362 P. 2d at page 603, the argument is:

> "that the contract has established the correlative rights of the parties, and that therefore, the state is powerless to prevent waste and drainage of gas as long as the monthly allowables are not unlawfully exceeded."

State orders and regulations relating to the conservation of gas and protection of correlative rights, of necessity, may often have, to a greater or lesser degree, some incidental effect on sales for resale in interstate commerce. And it may be conceded that such orders and regulations may at times so affect such sales as not to fall within the "production and gathering" exemption of Section 1 (b), *Cities Service Gas Co.* v. *State Corporation Commission of Kansas*, 355 U.S.

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[3] Much of the Federal Power Commission's Memorandum is devoted to an attack upon the level and the method of establishing production allowables. Since the orders establishing these allowables are not here under review, all arguments based upon their supposed invalidity are, of course, entirely irrelevant to the issue in the cas at bar.

391 (1958), but, we submit that to hold, as appellant and the Federal Power Commission would have this Court do, that pipeline purchasers of gas may preempt by contract the authority of the states so that they are powerless to enforce their legitimate orders and regulations to the extent that such orders and regulations affect the obligations of interstate pipeline purchasers under such contracts, is wholly and completely untenable. Such a holding would grant to interstate gas pipeline companies *carte blanche* to establish their rights and duties with respect to the conservation of gas and protection of correlative rights by private contract, free and immune from any regulation whatsoever by any duly constituted governmental authority, either state or federal.

CONCLUSION

We submit that it is abundantly clear, as established by the decisions of this Court, that the Natural Gas Act does not preempt the power of the oil and gas producing states to protect the correlative rights, *i.e.*, the property, of the owners of a common source of supply. We also submit, as has been shown above, that if the oil and gas producing states are to effectively implement this power so preserved to them, then they must also have the authority to require purchasers of gas to take proportionately from all wells to which they may be connected in a common source of supply even though the exercise of such authority by the states may affect, incidentally, sales of gas in interstate commerce. To hold otherwise will disturb, to the detriment of all, the existing federal-state relationship in the field of conservation by denying to the states authority to act in an area in which Congress has not empowered the Federal Power Commission to act.

For these reasons, we respectfully urge this Court to uphold appellee.

Respectfully submitted,

MID-CONTINENT OIL & GAS ASSOCIATION

By R. J. STANTON

W. W. HEARD
1107 Pan American Building
511 South Boston Avenue
Tulsa, Oklahoma

Attorneys for Mid-Continent Oil & Gas Association

November 12, 1962

APPENDIX A

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Before Commissioners: Joseph C. Swidler, Chairman; Howard Morgan, L. J. O'Connor, Jr., Charles R. Ross, and Harold C. Woodward.

Lone Star Gas Gathering Company) Docket No. CP62-179

Order Denying Petition for Leave to Intervene

(Issued October 17, 1962)

On March 5, 1962, Alamo Gas Supply Company (Petitioner) filed a petition for leave to intervene in the above-entitled proceeding which is upon an application for a certificate of public convenience and necessity filed by Lone Star Gas Gathering Company (Lone Star) pursuant to Section 7 (c) of the Natural Gas Act. By its application Lone Star seeks authorization to construct and operate pipeline facilities and to sell and deliver natural gas to United Gas Pipe Line Company in Victoria County, Texas, for transportation and sale in interstate commerce.

Petitioner is an intrastate gas company engaged in selling natural gas to the City of San Antonio, Texas. In its petition, Petitioner alleges that a portion of its gas supply comes from certain reservoirs partly under contract to Lone Star, and that, in the event a certificate is granted to Lone Star, the reserves dedicated to Petitioner are in danger of being drained by Lone Star. Petitioner alleges further that this situation thereby creates a conflict with respect to particular reserves dedicated to it and Lone Star and it cannot be assured of receiving its fair share of gas taken from the common reservoirs.

An answer to the petition was filed by Lone Star on March 12, 1962.

We have carefully considered the allegations of Petitioner and the answer thereto filed by Lone Star. The matters upon which Petitioner desires to be heard in this proceeding relate to the ratable production of natural gas, the correlative rights of producers and proration of production among producers producing natural gas from common reservoirs. We are of the opinion that these are matters which lie within the sphere of state control and cannot constitute a basis for intervention in the proceedings before this Commission.

The Commission finds:

Alamo Gas Supply Company has not shown that its participation in this proceeding is in the public interest or that the matters set forth in its petition affect interstate commerce or can properly be considered by the Commission in determining the merits of an application for a certificate of public convenience and necessity.

The Commission orders:

The petition for leave to intervene filed by Alamo Gas Supply Company be and it hereby is denied.

By the Commission.

/s J. H. Gutride
Joseph H. Gutride
Secretary.